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The Association of Investment Companies

# Practical recommendations to assist investment company boards in complying with the statutory rules on directors' general duties

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Part 3 of AIC Members' Guide to  
implementing the Companies Act 2006

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## To discuss the issues raised in this paper please contact:

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**Alison Andrews**

Project Manager, Technical Team  
E-mail: [alison.andrews@theaic.co.uk](mailto:alison.andrews@theaic.co.uk)  
Tel: 020 7282 5613

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## Introduction

Following the AIC's successful seminar on 17 April 2008 covering directors' general duties and liabilities under the new Companies Act 2006, the AIC has produced this summary of the main practical recommendations made by the speakers to assist investment company boards and their company secretaries in complying with these rules.

There are seven statutory general duties placed on directors under Part 10 of the Companies Act 2006, four of which came into force on 1 October 2007 and the rest, all relating to conflicts of interest, are effective from 1 October 2008. The following practical recommendations were made by Scott Cochrane of Herbert Smith LLP, Victoria Younghusband of SJ Berwin LLP and Ronald Paterson of Eversheds LLP during their presentations. A copy of the speakers' slides can be found on the AIC's website at [www.theaic.co.uk/files/other/aicseminarslides17april2008.pdf](http://www.theaic.co.uk/files/other/aicseminarslides17april2008.pdf).

### Actions required before 1 October 2008

- Articles of Association

The board should review the provisions within the company's Articles of Association and consider making any necessary arrangements for amendments to be made to give the directors power to authorise conflicts of interest. The board should consider whether it is necessary to call an EGM to approve the changes or whether the matter can wait until the next AGM. The changes to the Articles should be effective on and from 1 October 2008 (when section 175 comes into effect).

- Authorisation of conflicts of interest and updating declarations of interest

The company secretary should write to all directors well in advance of the introduction of the new regulations on conflicts of interest (section 175) on 1 October 2008, say by the end of August 2008, to ask directors to consider and report back on any conflicts of interest they have now or expect to have on or after 1 October. The directors should be asked to prepare a list of any positions and directorships they hold, and where appropriate any positions and directorships held by connected persons, that could put them in a position where their own interests may conflict with those of the company. They should also be asked to update the declarations of interest that they have previously made, either on first appointment or subsequently, as section 177, which also comes into effect on 1 October 2008, requires declarations of the **extent** of any interest in a transaction or arrangement with the company and not just the nature of such an interest.

- Review of decision-making process

The board might consider that it is an appropriate time to undertake a review or 'audit' of how board decisions are taken to ensure that processes are consistent with the requirements relating to directors' general duties under the Companies Act 2006. Alternatively the directors might ask the company

secretary to carry out a review and to report back to the board. Such a review could cover the process of preparing internal documentation and the administrative arrangements for board meetings.

- Training

It is recommended that board members are given training on their general duties under the Companies Act 2006. It is also important that the company secretary and the administrators are fully aware of the directors' duties, particularly with regard to the preparation of the meeting documentation.

- Directors' and officers' insurance policy

Given the new regulations on directors' liabilities contained in the Companies Act 2006, boards may consider it an appropriate point in time to review the terms of their D&O insurance policies, particularly with a view to identifying any inappropriate exclusions and ensuring cover includes the new type of derivative claims which came into existence on 1 October 2007.

### Processes to be put in place before 1 October 2008

- Preparation of board papers and board minutes

From 1 October 2007, directors have a duty to act in the way they consider, in good faith, would be most likely to 'promote the success of the company for the benefit of its members as a whole' and in doing so must have regard to six factors which are set out in section 172 of the Companies Act 2006 (and any other relevant factors). The board should consider the most appropriate way to record its consideration of the necessary factors as part of its formal decision-making process and put the necessary procedures in place.

It is recommended that, for each formal decision, a briefing paper is prepared in advance of each board meeting, usually by the company secretary or the investment manager and possibly with the help of advisers, which sets out all the issues which the directors are likely to take into account in making their decision, including the factors listed in section 172. Where one or more of these factors are not relevant, it is not considered necessary to include a negative statement in the briefing paper. The formal board minutes can then be limited to recording the fact that the briefing paper was presented to, and considered by, the board, and the decision reached.

- Procedures to authorise conflicts of interest

It is recommended that documentation and processes are put in place to create and maintain a formal list of authorisations which have been granted by the board on and after 1 October 2008 (in addition to the list of directors' interests in transactions with the company to be maintained under section 177). The board should consider the most suitable way to keep this list up to date. For example, the chairman might consider including a reminder, perhaps by way of an agenda item, at every board meeting to regularly ask directors to disclose any relevant changes to their position or those of their connected persons which need to be authorised by the directors.

- Policy and procedures for dealing with a real conflict of interest

The board should set out its policy and put procedures in place for dealing with a situation where a real conflict of interest arises after board authorisation has been given under the new rules. The policy could cover the options available to the board, which include withholding information from the director concerned, excluding him/her from the board meeting or part of the meeting, or asking the director concerned to resign.

- Procedure for reporting to shareholders on conflicts of interest

The board might want to put a process in place to give assurance to shareholders that the authorisation power regarding conflicts of interest given to the directors by the shareholders is being properly exercised, perhaps by including a statement in each annual financial report.

- Training for new directors

The chairman and the company secretary should consider what form of training could be given to new directors joining the board to inform them of their legal duties, including their general duties under the Companies Act 2006, and put the necessary procedures in place to achieve this. A reference to the legal requirements should also be included in the terms of appointment.

### Actions required on 1 October 2008

- Authorisation of conflicts of interest

It is recommended that directors hold a board meeting on or as near as possible after 1 October 2008 to authorise potential conflicts of interest. Under the implementing regulations, section 175 only applies where the conflict or potential conflict situation arises on or after 1 October 2008 and so strictly speaking board authorisation should only deal with new situations, or an existing situation which does not amount to a conflict prior to 1 October, but which may develop into a conflict after 1 October. However, boards may take the view that they will authorise existing situations on the basis that is better to do so than not, given that the impact of section 175 on existing situations is not clear.

Given the importance of this matter, it is recommended that a full board meeting is held, rather than authorisation being delegated to a sub-committee of the board, although a sub-committee could be used initially to review the authorisations and made recommendation to the board.

### Ongoing reviews

- Compliance review

The board might consider undertaking a regular review of its continued compliance with the seven general directors' duties set out in the Companies Act 2006. This might be an annual review timed to coincide with the preparation by the directors of the business review. The business review forms part

of the annual financial report and is designed to help shareholders assess how the directors have performed their duty to promote the success of the company.

- Review of authorised conflicts of interest

It is recommended that the list of authorised conflicts of interest is reviewed regularly by the board, or by a committee of the board which then makes a report to the board, to ensure that it is appropriate for the relevant matters to remain authorised. This might be done annually as part of the board evaluation process.

### Further information

Further information on directors' general duties under the Companies Act 2006 can be found in guidance produced by the Institute of Chartered Secretaries and Administrators. Appendix A of this guidance contains a useful paper by the GC100 on directors' duties. This guidance can be found on the ICSA's website at [www.zoomerang.com/Survey/survey-intro.zgi?p=WEB227BLF2A2BG](http://www.zoomerang.com/Survey/survey-intro.zgi?p=WEB227BLF2A2BG) (note that access is subject to free registration).

Further information on conflicts of interest under the Companies Act 2006 can be found in the GC100's paper on directors' conflicts of interest which can be found at [www.theaic.co.uk/files/other/AICSeminarGC100%20Paper.pdf](http://www.theaic.co.uk/files/other/AICSeminarGC100%20Paper.pdf).

### Auditor liability limitation agreements

One of the speakers at the seminar discussed the issue of auditor liability limitation agreements. The FRC has published draft guidance and a consultation document on this issue (the consultation closed on 14 March 2008) which can be found on its website at [www.frc.org.uk/about/auditorliability.cfm](http://www.frc.org.uk/about/auditorliability.cfm). Final guidance is expected in the first half of 2008.





**Association of Investment Companies**

24 Chiswell Street  
London EC1Y 4YY

Telephone 020 7282 5555

Fax 020 7282 5556

[enquiries@theaic.co.uk](mailto:enquiries@theaic.co.uk)

[www.theaic.co.uk](http://www.theaic.co.uk)

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